

Choice of Entity for undertaking Non Banking Businesses

Chapter III B of RBI Act, 1934 clearly indicates that an entity being a Non Banking entity, in order to undertake the activities prescribed for a Financial Institution including acceptance of deposits, shall be created as a ***Company or Corporation incorporated under Companies Act, 2013***, and would be termed as an Non Banking Financial Company (NBFC). Any other form of entity like an individual or partnership firm or unincorporated body or Association of Persons (AoP) etc are prohibited from undertaking financial businesses as prescribed in the Act as their Principal Business Activity specifically by accepting deposits from public.

A Limited Liability Partnership (LLP) though being defined as a 'body corporate' under LLP Act, 2008 cannot undertake NBFC business as it is not a Company registered under Companies Act, 2013 or a Corporation or Cooperative Society or an unincorporated body as defined under RBI Act, 1934 and is prohibited from accepting public deposits. There have been instances in 2010 post introduction of LLP laws, whereby finance companies wanted to get converted into LLPs to enjoy taxation benefits and RBI objected to issuing No-objection certificates for this purpose as required by the Ministry of Corporate Affairs. There is also a notification issued by RBI on 30 March 2013 prohibiting NBFCs from associating with or contributing to capital or becoming partners in partnership firms. Further clarification was issued that this prohibition extends to LLPs and AoPs too. This confirms the aspect that LLPs cannot undertake NBFC business or be associated with any NBFC. RBI has also proposed that RBI Act, 1934 be suitably amended to include LLPs as unincorporated bodies for the purpose of being prohibited from acceptance of public deposits.

A Non Banking Institution (NBI) could be a ***State Finance Corporation*** as defined under The State Financial Corporations Act, 1951 incorporated as a company under Companies Act, 1956/ 2013. Some of the NBIs under this category are Kerala State Power & Infrastructure Finance Corporation Ltd, West Bengal Industrial Development Corporation Ltd, West Bengal Infrastructure Development Finance Corporation Ltd, Tamil Nadu Industrial Development Corporation Ltd etc. Though these NBI are governed by the respective State Governments and not directly governed by RBI, their deposit acceptance activities are regulated by RBI.

An NBI could be a ***Public Financial Institution (PFI)*** as defined under Sec 2(72) of Companies Act, 2013. An NBI is also termed as Development Financial Institution (DFI) which should be a body corporate; incorporated/established under a Special Central or State Act, or, not less than 51% of the paid-up share capital is held or controlled by the Central Government or by any State Government or Governments or partly by the Central Government and partly by one or more State Governments. Such NBI should not conduct Banking business but be registered as an NBFC with RBI. It is to be noted that not all PFIs are NBIs. Also, though NBIs are registered as NBFCs with RBI, still they are not fully regulated by RBI as these are ***Government Companies***. Some of the Non deposit accepting NBFCs falling under this category are India Infrastructure Finance Company Ltd (IIFCL), Irrigation and Water Resources Finance Corporation Ltd

(IWRFC), Infrastructure Development Finance Corporation Ltd (IDFC) and Industrial Finance Corporation of India Ltd (IFCI). There are also certain Specialized All-India Financial Institutions which are NBFCs - like Tourism Finance Corporation of India Ltd (TFCIL), Rural Electrification Corporation Ltd (REC), Power Finance Corporation Ltd (PFC).

An NBI could be a **Cooperative Credit Society** registered under The Cooperative Societies Act, 1912. A Society cannot however be registered as an NBFC as it is not a Company under Companies Act, 2013 and hence is not regulated by RBI. These societies are regulated by respective State Government enactments and may conduct financial activities which are non-banking in nature. RBI prohibits such societies from accepting public deposits but does not prohibit acceptance of deposits from its members.

Currently RBI regulates four All-India Term Lending and Refinancing Institutions which are Development Banks and not NBIs - National Bank for Agriculture and Rural Development (NABARD), Small Industries Development Bank of India (SIDBI), Export Import Bank of India (EXIM Bank) and National Housing Bank (NHB). It is to be noted that though these Financial Institutions are Banks, NABARD created through the NABARD Act, 1981 - regulates Societies which undertake the business of Micro Finance Institutions and NHB created through NHB Act, 1987 - governs activities of NBFCs which are Housing Finance Companies like Housing and Urban Development Corporation Limited (HUDCO) etc.

It is therefore clarified beyond doubt that only a Company incorporated under Companies Act, 1956/ 2013 can be an NBFC and hence there is no question of choice of entity for a businessman willing to choose this area of operation.